In the Supreme Court of the United States

OCTOBER TERM, 1924

WILLIAM H. EDWARDS, COLLECTOR OF Internal Revenue, Second New York District, petitioner
v.
CHILE COPPER COMPANY
No. ———

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

The Solicitor General, on behalf of William H. Edwards, Collector of Internal Revenue for the Second New York District, prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Second Circuit, rendered on February 16, 1925, affirming the judgment of the District Court for the Southern District of New York.

STATEMENT OF THE CASE

This action was brought by the Chile Copper Company against the Collector to recover $213,188.64, with interest, the amount of capital-stock taxes alleged to have been erroneously collected by petitioner from the respondent for the years 1917

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to 1920, inclusive. The Collector moved for judgment dismissing the complaint upon the ground that it did not state facts sufficient to constitute a cause of action. The District Court, Judge Learned Hand presiding, denied the motion and granted judgment for the plaintiff for the full amount. (Rec. p. 88, 294 Fed. 581.)

Upon writ of error the Circuit Court of Appeals affirmed the judgment in a memorandum opinion, stating merely that the judgment of the lower court was affirmed.

THE QUESTION INVOLVED

The question involved is whether the Chile Copper Company was, during the years in question, "doing business" within the meaning of the provisions of Section 407 of the Revenue Act of 1916 and Section 1000 of the Revenue Act of 1918. The courts below held that it was not.

THE STATUTES

Section 407 of the Revenue Act of 1916, Act of September 8, 1916, Ch. 463, 39 Stats. 756, 789, so far as is relevant, provides as follows:

> SEC. 407. That on and after January first, nineteen hundred and seventeen, special taxes shall be, and hereby are, imposed annually, as follows, that is to say:
>
> Every corporation, joint-stock company or association, now or hereafter organized in the United States for profit and having a capital stock represented by shares, and

every insurance company, now or hereafter organized under the laws of the United States, or any State or Territory of the United States, shall pay annually a special excise tax with respect to the carrying on or doing business by such corporation, joint-stock company or association, or insurance company, equivalent to 50 cents for each $1,000 of the fair value of its capital stock and in estimating the value of capital stock the surplus and undivided profits shall be included: * * * *And provided further,* That this tax shall not be imposed upon any corporation, joint-stock company or association, or insurance company not engaged in business during the preceding taxable year, * * *.

Section 1000 of the Revenue Act of 1918, Act of February 24, 1919, Ch. 18, 40 Stats. 1057, 1126, so far as relevant, provides as follows:

SEC. 1000. (a) That on and after July 1, 1918, in lieu of the tax imposed by the first subdivision of section 407 of the Revenue Act of 1916—

(1) Every domestic corporation shall pay annually a special excise tax with respect to carrying on or doing business, equivalent to $1 for each $1,000 of so much of the fair average value of its capital stock for the preceding year ending June 30 as is in excess of $5,000. In estimating the value of capital stock the surplus and undivided profits shall be included;

* * * * *

(c) The taxes imposed by this section shall not apply in any year to any corporation which was not engaged in business (or in the case of a foreign corporation not engaged in business in the United States, during the preceding year ending June 30, * * *.

THE FACTS

The Chile Copper Company is a corporation of the State of Delaware with capital stock outstanding of the par value of $95,000,000. (Rec. p. 4.)

The Chile Exploration Company is a corporation of the State of New Jersey, with capital stock outstanding of the par value of $1,000,000, and its principal business has been the mining of copper from property in the Republic of Chile owned by it. Since its incorporation the Chile Exploration Company could not at any time have developed its mining property without borrowing large sums of money, and in order to borrow the necessary money it would have been necessary to sell bonds or other obligations secured by mortgage upon its property, but the laws of Chile provided that mining property in that country could not be sold for debt so as to vest title thereto in creditors. Therefore the Chile Exploration Company would have been unable effectively to mortgage its mining property so as to secure an issue of its obligations, and unsecured obligations would not have been salable in investment markets. (Rec. p. 5.)

To meet this difficulty the Chile Copper Company was organized for the principal purpose of providing a means whereby money could be borrowed from investors in sums sufficiently large to develop property of the Chile Exploration Company. The Chile Copper Company accordingly was organized on April 16, 1913, to hold the capital stock of the Chile Exploration Company and pledge such stock as security for the bond issues, the proceeds of which should be used, loaned, and advanced from time to time to furnish the necessary capital to develop the mining property of the Chile Exploration Company. (Rec. p. 6.)

At all times mentioned in the complaint the Chile Copper Company owned all the stock of the Chile Exploration Company, and on April 1, 1917, it pledged that stock to the Guaranty Trust Company under an agreement between the Trust Company, the Chile Copper Company, and the Chile Exploration Company as security for an issue of bonds. (Rec. p. 6.)

The Trust Agreement provided, among other things, that the proceeds of the bonds should be used only to pay off certain existing indebtedness and for the acquisition, construction, or improvement of property necessary or useful in connection with the mining, refining, or marketing of copper or copper ore derived from property owned by the Chile Exploration Company. (Rec. pp. 6 and 7.)

In addition, a certain other issue of bonds made in the year 1913 was still outstanding in the year 1917. (Rec. p. 7.)

The plaintiff alleges (Par. VII, Rec. p. 7 *et seq.*) that during the period from January 1 to June 30, 1917, the activities of the Chile Copper Company "without any omissions or exceptions, consisted solely of the following." These activities are then set forth at length and may be summarized as follows:

(1) Stockholders' and directors' meetings were held, directors and officers were chosen, corporate books and accounting records were kept, and an office was maintained and whatever was necessary to maintain the corporate existence and organization was done.

(2) The Chile Copper Company owned and voted the entire capital stock of the Chile Exploration Company, and thus selected directors of that company, but it did not act as purchasing or selling agent for that company.

(3) It paid the interest on $15,000,000 worth of bonds secured by a pledge of the entire capital stock of the Chile Exploration Company, the proceeds of which had been paid to that company as an additional investment in that company. It authorized a further issue of bonds of the par value of $100,000,000, to be secured by a pledge of the entire capital stock of the Chile Exploration Company, and executed an appropriate trust agreement. It executed an agreement with under-

writers and issued bonds of the par value of $35,000,000. It received payment upon said bonds from subscribers, which was deposited in a special account with the Guaranty Trust Company, and it paid the expenses of the bond issue and made provision for the accrued interest payable upon the bonds. (Rec. p. 8.)

No part of the proceeds of the bond issue was used to pay the floating indebtedness of the Chile Exploration Company or for the acquisition of property by the Chile Copper Company, but the entire proceeds were used to pay the floating debt of the Chile Copper Company or were advanced or held for future advance to the Chile Exploration Company. (Rec. pp. 9 and 10.)

(4) It received from the Chile Exploration Company payments of interest upon loans previously made, and also payments on account of a dividend, and interest-bearing notes in payment of previous loans and of a portion of the bond discount incurred in marketing the 1917 bond issue. (Rec. p. 10.)

(5) It made loans on open account to the Chile Exploration Company. (Rec. p. 10.) It furnished to the Guaranty Trust Company statements showing the application of the proceeds of checks drawn against the proceeds of the bond issue. (Rec. p. 11.)

The activities of the Chile Copper Company during the succeeding years are set forth under the different causes of action for each year and did not

differ materially from those heretofore summarized. The amount advanced by the Chile Copper Company to the Chile Exploration Company for the year ending June 30, 1917, was $1,250,000. (Rec. p. 11.) For the next year it was $3,500,000. (Rec. p. 20.) For the next year it was $7,136,000. (Rec. p. 29.) For the next year it was $700,000. (Rec. p. 41.)

In addition it invested some of its surplus funds received from the bond issue in Liberty Bonds (Rec. p. 41) and also loaned a large amount of said surplus on call loans through the Guaranty Trust Company and the Central Union Trust Company. During the year ending June 30, 1920, 224 loans aggregating $37,200,000, were made, and 180 loans aggregating $29,100,000 were called or paid. During the year ending June 30, 1920, the plaintiff received $332,366.90 interest on said loans. (Rec. p. 42.) During the year ending June 30, 1919, a portion of its surplus funds was invested in Liberty Bonds and United States Certificates of Indebtedness, and 141 call loans aggregating $26,045,000 were made, upon which it received interest amounting to $194,579.20. (Rec. pp. 30, 31.)

The Chile Copper Company claims that these activities did not constitute doing business, and the courts below have so held. The Government claims that such holding was erroneous.

REASONS FOR GRANTING THE WRIT

I

The Circuit Court of Appeals erred in holding with the District Court that the Chile Copper Company was not doing business within the meaning of the statutes involved.

The question of what constitutes doing business has been before this Court several times in cases arising under the Corporation Excise Tax of 1909, Act of August 5, 1909, Ch. 6, 36 Stats. 11, 112. *Flint* v. *Stone-Tracy Company*, 220 U. S. 107; *Zonne* v. *Minneapolis Syndicate*, 220 U. S. 187; *McCoach* v. *Minehill & Schuylkill Haven Railroad Company*, 228 U. S. 295; *United States* v. *Emery, Bird, Thayer Realty Company*, 237 U. S. 28; *Von Baumbach* v. *Sargent Land Company*, 242 U. S. 503.

In the *Von Baumbach case* this Court reviews its decisions in the preceding cases.

Of the *Zonne case*, Mr. Justice Day, writing for the Court, said that the Court decided that the corporation concerned "was not engaged in doing business within the meaning of the act, by reason of the fact that the corporation had practically gone out of business and had disqualified itself from any activity in respect thereto." (242 U. S. 515.)

Of the *McCoach case* Mr. Justice Day said "that a corporation which had leased all its property to another, and was doing only what was necessary to

receive and distribute the income therefrom among stockholders, was not doing business within the meaning of the Act." (242 U. S. 515–516.)

Of the *Emery, Byrd, Thayer Realty Company case,* he said:

> * * * this court held that a corporation which merely kept up its organization, distributing rent received from a single lessee, was not doing business within the meaning of the act. (242 U. S. 516.)

And in the *Von Baumbach case* the rule to be observed was stated as follows (242 U. S. 516):

> The fair test to be derived from a consideration of all of them is between a corporation which has reduced its activities to the owning and holding of property and the distribution of its avails and doing only the acts necessary to continue that status, and one which is still active and is maintaining its organization for the purpose of continued efforts in the pursuit of profit and gain and such activities as are essential to those purposes.

Applying this rule, it is perfectly evident that the Chile Copper Company was doing business, was maintaining its organization for the purpose of continued efforts in the pursuit of profit and gain, and such activities as were essential to those purposes. The purpose of its organization was to do those things which were essential to the continued operations of the Chile Exploration Company, because the latter company would otherwise

be unable to operate effectively. Its object was to secure capital by borrowing money upon its bonds and to that end conduct the negotiations, procure appropriate agreements, and do the other things necessary to make the bonds salable; and thereafter to see that the proceeds of the bonds were applied in accordance with the agreement made between itself, the Chile Exploration Company and the Trustee. In a sense it might be said that it became the financial agent for the Exploration Company, yet that would hardly be accurate, for, considering the practical realities of the situation, the Exploration Company should rather be regarded as the agent of the Chile Copper Company. The control was in the Chile Copper Company through its ownership of all the stock of the Exploration Company. It procured the capital, it pledged its credit, and mortgaged its property for that purpose. It obligated itself to see that money thus raised was used in accordance with the agreement made with those who bought the bonds. It was the active not the passive party. While in strict contemplation of law the Exploration Company could hardly be said to be the agent of the Copper Company, nevertheless the latter company directed its operations and received the profit therefrom.

It furnished the money and put that money to work through the Exploration Company.

In addition to all this, it was actively engaged in another special line of business, the business of loaning money on call, and it also was investing its

surplus funds in United States securities. Can it be said that a company which borrowed huge sums of money to pay its own floating indebtedness and to furnish the working capital for another company whose entire stock it owned; which was loaning millions of dollars in the money market and which received by way of interest from such loans in one year over $300,000, had " practically gone out of business " and " disqualified itself from any activity in respect thereto " (the *Zonne case*), or " was doing only what was necessary to receive and distribute the income therefor among stockholders " (the *McCoach case*), or was " merely keeping up its organization, distributing rent received from a single lessee " (the *Emery Bird, Thayer Realty Company case*)? Was it not rather one which is " still active and is maintaining its organization for the purpose of continued efforts in the pursuit of profit and gain and such activities as are essential to those purposes " (the *Von Baumbach case*)? We contend, therefore, that the decision of the courts below was directly contrary to the controlling decision of this Court in *Von Baumbach* v. *Sargent Land Company* (242 U. S. 503).

Judge Hand, in his opinion in the District Court (Rec. p. 88), refers to a number of cases which have been decided in the lower Federal courts which we deem it unnecessary to consider in detail. There are numerous other cases in the District Courts which seem to indicate a reluctance on the part of those courts to accept what the Government

thinks is the meaning of the decision of this Court in the *Von Baumbach case.* So far as we know there is no case yet decided which involves facts in any way closely analogous to those in the present case.

II

The amount involved in this case, including interest and costs, is $269,710.73, and many other cases are pending involving very large sums of money, the decision of which will depend upon the decision of this case, which makes it one of great public interest and of great importance to the Treasury of the United States in the administration of its revenue laws.

The principle involved is one concerning which there has been much diversity of opinion in the lower courts, and no settled rule seems yet to have been established which has been accepted by the lower courts.

For these reasons it is respectfully submitted that the petition for a writ of certiorari should be granted.

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APRIL, 1925.

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